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Willow Valley Club Association

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Arizona Corporation Commission
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SEP 13 2013

September 13, 2013

Chairman Stump and Commissioners
1200 W. Washington St.
Phoenix, Arizona 85007

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Re: Willow Valley System Improvement Benefits Mechanism
Docket No. W-01732A-12-0315 (consolidated with W-01212A-12-0309,
SW-20445A-12-0310, W-03720A-12-0311, W-02450A-12-0312,
W-02451A-12-0313 and W-02446A-12-0314)

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Dear Chairman Stump and Commissioners,

I am the President of the Willow Valley Club Association (the "Association"). The Association has approximately 1,600 members most of whom receive water service from the Willow Valley Water Company ("Willow"), a division of Global Water Resources, LLC ("Global"). We have intervened in the above referenced rate case. Unfortunately, our limited finances, as well as an annual expenditure limitation imposed by our Articles and By-laws, left us with a modest budget of \$5,000 for this matter. Obviously, such limited funding made it impossible for the Association to actively participate in this matter involving multiple Global utilities owned by Global. We did have legal counsel review the Company's Application, as well as Staff's and RUCO's direct testimony as it related to the Willow Valley System. Counsel also attended settlement discussions on our behalf and has discussed Willow's request for a System Improvement Benefits ("SIB") Mechanism with us and Willow.

We lack funding and expertise to actively participate in the hearing scheduled for September 19, 2013 on Willow's proposed SIB Mechanism. In lieu of pre-filed testimony, I have prepared and file this letter to relate the Association's general opposition to Willow's request for a SIB in this case.

I do not plan to be physically present during the September 19, 2013 hearing, but, if requested, can be available by phone to answer questions regarding this letter.

The Association Supports System Improvements

The Association agrees that there is a need for system improvements and that the improvements Willow has identified should be made by Willow. The Association is unable to evaluate whether the proposed projects are in the appropriate priority or whether the cost estimates are appropriate.

Chairman Stump and Commissioners
Willow Valley Water

The fundamental question before the Commission is whether Willow has demonstrated, on this record, that the SIB mechanism it is now proposing is both warranted and appropriate. The Association does not believe such a showing has been made and that Willow and its parent should make the improvements and seek to recover a return thereon under the traditional ratemaking process.

Willow Has Not Demonstrated A SIB Mechanism Is Appropriate

We understand a SIB Mechanism is intended to encourage the utility to invest in water infrastructure where the normal ratemaking process has proved to be inadequate and to help to alleviate rate shock. The Association agrees with both objectives, but asks where is the evidence in this record that demonstrates a SIB Mechanism is needed for the Willow system.

No Extraordinary Need For A SIB Has Been Shown

According to Mr. Fleming, Willow was in a poor and dilapidated state when acquired by Global in 2006 requiring significant improvements to the water treatment system and the replacement of nearly the entire distribution system. Thus, this is not a new issue and should have been considered when Global acquired the system. The condition of the Willow system alone, therefore, does not justify the special ratemaking treatment of a SIB Mechanism, especially where the company has already received and is currently requesting significant increases in its rates (a 90.4% increase in 2010 and another 57.53% increase under the Settlement Agreement).

Mr. Fleming testifies that Global has significantly invested in the Willow system without a SIB Mechanism, primarily on treatment related improvements. He does not indicate that Global is financially unable to make further capital improvements, or threaten to stop doing so, if no SIB Mechanism is approved. This testimony does not justify approving the SIB Mechanism for the Willow system. And why is the Willow system being singled out for this extraordinary mechanism? Global has testified that some of its other systems also are in need of significant overhaul.

We understand the Settlement is designed to provide Willow \$170,922 of return (Settlement A-1), plus \$285,596 in depreciation expense (Settlement C-2). The Association recognizes that due to the phase-in, rates are now not designed to generate these dollars until 2016. However, even after deducting the negative test year return of (\$71,868), Willow continues to have \$213,828 in depreciation dollars during the test year and on an ongoing basis until the rates start to generate positive return dollars. These depreciation dollars alone will generate more than \$1,069,140 over the next 5 years for Willow. According to Mr. Lin, the projects Willow has identified for the SIB Mechanism are estimated to cost a total of \$876,233 and will be spread out over the next 5 years. In four out of the five years the annual expenditure on SIB projects will be less than the depreciation dollars available. In the one year where the improvement will cost more than the amount of depreciation dollars being generated, the cost will require Willow to invest just another \$1,000. Willow has identified no other capital projects where these depreciation dollars will be expended over the next five years.

Chairman Stump and Commissioners
Willow Valley Water

Willow should be required to expend the funds included in rates for depreciation expense on capital projects before it is entitled to recover a return outside of a full rate case through a SIB Mechanism. Yet, Willow requests a surcharge, in between rate cases, to recover a pre-tax return (i.e., the return plus the tax impact) and additional depreciation expense on improvements it could readily make with the depreciation dollars generated by existing rates. Neither Willow nor Staff have justified such extraordinary ratemaking treatment in this case.

What Rate Shock Is Avoided?

Decision No. 71878 dated September 14, 2012 granted Willow a 90.40% increase in revenues based upon a 7.6% return on a Fair Value Rate Base of \$2,278,955 without any special downward adjustment for the condition of the distribution system. The Settlement Agreement proposes another 57.53% increase in revenues based upon a 7.5% rate of return on a Fair Value Rate Base of \$2,251,164. The Association agrees that these two rate cases have resulted in rate shock to Willow's customers. Thankfully, the shock will be softened by phasing in this latest increase. The benefit of the phasing will be adversely impacted if SIB surcharges are added to the rates while they are being phased-in.

Neither Willow nor Staff has discussed the level of estimated surcharge that will be requested after the completion of each phase of SIP improvements. Nor have they discussed the specifics of how those surcharges will impact Willow's customers or how inclusion of these specific projects in a SIB Mechanism will help to avoid rate shock for Willow customers. The Association believes it is impossible for the Commission to evaluate the need and appropriateness of the SIB Mechanism for Willow without this specific information before it.

Lack of a Tariff and a Plan of Administration

Willow has done little to describe the SIB mechanism itself, relying instead on the description of the SIB mechanism approved for Arizona Water Company by Decision No. 73938. Willow has neither submitted a form of SIB Tariff or a plan of administration to support its proposed SIB Mechanism. How will Willow customers understand the purpose and mechanics of the SIB Mechanism without such documentation readily available for their review? Willow customers should not be required to read an entire rate decision involving several different water systems and/or the Arizona Water Company decision to understand how the SIB mechanism for the Willow system works.

Some Options

The Association believes Willow has failed to justified implementing a SIB Mechanism at this time. If the Commission disagrees and still intends to approve one, we ask that the following conditions be imposed beyond those suggested by Willow:

1. The SIB Mechanism be set forth in a separate tariff, together with a Plan of Administration;
2. No SIB surcharge be imposed until 2016 – after the current rates are fully phased-in;
3. The estimated cost submitted for a project be the maximum Willow can request for SIB treatment;

Chairman Stump and Commissioners
Willow Valley Water

4. Willow be required to demonstrate that the dollars received as depreciation expense are being placed back into plant, or held in reserve for that purpose as part of the SIB evaluation; and
5. Willow not seek another rate increase, other than the SIB mechanism until 2017 based upon a test year no later than December 31, 2016.

The Association and I appreciate the opportunity to submit this letter setting forth our position on the SIB Mechanism being proposed by Willow. I ask that the letter be entered into evidence on behalf of the Association during the hearing scheduled for September 19, 2013.

Sincerely



Gary McDonald, President
Willow Valley Club Association

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